

DEMONETIZATION AND ITS EFFECT ON BANKING SECTOR

Padmavathi Agarwal¹ & B. Bhagavan Reddy²

¹*UGC Post Doctoral Fellow, Department of Commerce, S.V.U. College of Commerce, Management & Computer Science, Sri Venkateswara University, Tirupati, Andhra Pradesh, India*

²*Former Dean, Faculty of Commerce & Management, S.V.U. College of Commerce, Management & Computer Science, Sri Venkateswara University, Tirupati, Andhra Pradesh, India*

Received: 23 Jan 2018

Accepted: 21 Feb 2018

Published: 26 Feb 2018

ABSTRACT

Demagnetization is a tool to battle inflation, black money, corruption and crime, discourage cash transactions and help trade. The banning of Rs. 500 and Rs.1000 currency notes has influenced almost all sections in all the corners of the economy. Its effect on banking sector is significant as the bank is a center to channelize the legal tender money to the needs of the society. The biggest beneficiaries of demagnetization are banks. It made the banks to accept the deposits without any cost of promotion and drastically increased liquidity position of banks. The present study is made out of the available literature in the post demonetization. It portrayed the effect of demonetization on the banking sector.

KEYWORDS: Reserve Bank of India (RBI), Government of India, Cash Reserve Requirement (CRR), Demonetisation, Liquidity, Green Banking and Digitalisation

INTRODUCTION

Banks are core part of any economy. They channelise the money for the smooth functioning of different sectors. Initiative of green banking has made the banks to transform conventional banking services into modern ones. The products and services are offered through electronic devices with the help of internet. Surgical strike on black money called 'demonetisation' brought enormous changes in all the sectors of the economy. Banks are not exceptions to the influence of demonetization and brought vibrations in the operations as well as products and services of banks. It created greater demand for digital banking services where cashless transactions are prioritized. Day to day operations of banks are affected and led to liquidity management a difficult task. The exchanging of banned currency notes eroded the quality of service. At the same time, meeting of the Reserve Bank of India (RBI) was challenging. Demonetization has disturbed the bank operations and made the employees to work under unconditional stress with the extended working hours. Most of the banks were unable to discharge other banking services effectively while exchanging the banned currency notes. Hence, the present study is made to figure out the influence of demonetization on the banking sector. It highlights the post demagnetization effect on banks and their operations.

REVIEW OF LITERATURE

Nithin and Sharmila have opined that demonetization has a short-term negative impact on different sectors of the economy and solved when the new currency notes are widely circulated. They also argued that the government should clear all the problems arose out of demonetization and help the economy to work smoothly. Nikita Gajjar, deliberated a

study on "Black Money in India: Present Status and Future Challenges and Demonetisation." In addition, described the framework, policy options and strategies that Indian Government should adopt to tackle the present and future challenges. Vijay and Shiva have examined demonetization and its complete financial inclusion. The rewards of demagnetization are many encouraging and it is in the long-term interest of the country. Moreover, viewed that it had given temporary pain but it taught financial lessons. It has influenced the banking sector to invest considerably on digitalisation of banking services. Manpreet Kaur has conducted a study on demonetization and the impact on cashless payment system. The cashless system in the economy has many fruitful benefits less time-consuming, less cost, etc. The author has expected that the future transaction system in all the sectors is cashless. Likes Ike has researched on demonetization and its positive and negative impact. The main purpose of it is to eradicate the black money and diminish the corruption. He has opined that the Government of India has become successful to some extent. Demonetization had a negative impact for a short duration and the real impact will be known in future. Soweto Singhal has organized a study on demonetization and e- banking in the country. It is organized to ascertain the awareness in the rural India. Awareness about e-banking facilities and how much it has increased after demagnetization with a sample of 100, an attempt is made to know the difference in the usage and awareness level between rural and urban public. It was found that urban male youth have higher awareness, usage of e banking etc.

METHODOLOGY OF THE STUDY

The study is based on secondary data. It includes available published literatures such as books, journals, newspapers and relevant government websites.

DEMONETIZATION

The term demonetization may be defined as a conclusion or the act of ending something; or "the termination of an agreement". The numbers and calculations for this are overwhelming. According to RBI, there are 16.5 billion '500 - rupee' notes and 6.7 billion '1000 - rupee' notes were in circulation. Of this, Rs. 500 notes constitute 45 per cent, while Rs.1000 notes, 39 per cent in value terms. However, Rs. 10 and Rs. 100 notes constituted 53 per cent of notes in circulation. The financial action task force has opined that there is a criminal use of the international financial system. In two words: black money. Unaccounted money, often used in any form of corruption or illicit deals, usually takes the form of high-value notes, which in this case are Rs. 500 and Rs. 1,000 notes.

DEMONETIZATION AND BANKING OPERATIONS

Banks are the backbone in the process and the biggest beneficiary. In the post exchange of currencies, banks had higher deposits and transaction volumes, lower cash handling costs and greater acceptance of digital channels. The influences were both short and long - term ones. In the short-term, it disrupted the banks and stressed strongly to carry out operations and in the long run, it helped the banks to pool the deposits without incurring any cost. Here are four influences of demonetization on banks.

Increase in Deposits

Demonetization has increased the deposits in banks. Unaccounted money in the form of Rs.500 and Rs.1000 were flowing to the banks and the sizes of deposits have increased. It helped the banks to increase their deposits.

Fall in the Cost of Funds

Over the past few months, deposits have increased. It led the banks to keep a major part of deposits in the form of cash deposits. Banks have a lion's share in deposits biggest gain with the rise in deposits and finally led to low cost funds.

Demand for Government Bonds

After sharp rise in deposits banks have lend such surplus deposits to the RBI under the reverse repo options. Public sector banks deployed excess funds in government bonds. The return on bond investment is likely to add 15 to 20 per cent increase in the earnings of banks.

Slugginess in Lending

The volume of lending has declined after demagnetization. This has an effect on the growth of deposit. Banks have tried to lend the money to the needy group with reduced interest rates, but shrunk over the last few months.

RESULTS OF POST- DEMONETISATION

The results of demonetization have a positive and negative impact on banks. They have influenced liquidity, profitability and so on.

Positive Results of Demonetisation

The pros of demagnetization are no more black money and legal transactions. The Government will easily find out who is holding black money. Banks will galore with deposits and liquidity is easily available at low rate of interest. Lowest interest means more investments and more employment. More business means more income through taxes, no cash crunch for welfare schemes, etc. The following are positive results of demonetization.

Free Flow of Deposits

Banks have gained deposits substantially after demagnetization, which they can invest in improving their liquidity and profitability.

Improved Digital Interface

Increased the use of digital tools and equipment while executing transactions in banks. This has led to decrease in cash loss, due to theft, dacoits and misappropriations.

People's Surplus at Bank

Cash is an idle asset, which does not yield any income unless kept in a bank. Therefore, demonetization has made the people to keep their surplus money in a formal institution to earn some sort of income.

Increased Number of Customers

Demonetization has influenced the public to deal with banks. It made even a non - income group to have an account. It has increased the number of account holders.

Negative Results of Post - Demonetisation

Demonetization has brought some operational issues to banks. It has disturbed employees, operational costs and profitability. The following are some of the cons of demonetization.

Cash Reserve Requirement

Hundred per cent CRR on incremental deposits meant that banks did not earn any interest on Rs. 3 lakh crore deposits for nearly a fortnight.

Waiver of ATM Charges

ATM charges were waived off during banned note exchange and banks incurred a loss of Rs. 20 in every transaction.

Waiver of Merchant Discount Rate

Banks have lost one per cent discount charge from merchants on every card transaction.

Non- Selling of Loans

Banks have focused on the exchange of currency notes. They were not able to sell loan products. This has reduced the lending activities.

Reduction in the Sales of SMEs

During demonetization, the business of certain small or medium - sized enterprises (SME's) had declined 50 - 80 per cent. Consequently, they could default in their installments due to the banks. This has led to growth in NPA's.

Stress on Employees

Bank employees were kept under pressure and overtime working. It has depressed them and brought imbalance in life style. The continuous notifications from RBI and the absence of money banks have faced the fury of customers. Bank staff was helpless when they did not receive enough cash to meet the demand for cash. Frequent changes in regulations and voluminous old notes have made the staff to handle customers with a smile and overtime without extra salary.

CONCLUSIONS

Demagnetization is a weapon used by government to fight against corruption and black money. At the same time, it has brought changes in all the corners of the economy. Demonetization has badly affected the banks. Banned denominations were ploughed back and allowed the citizens to exchange with the banks. While exchanging, it disturbed temporarily and influenced its regular operations. Though it affected to a greater extent, it has paved the economy to grow in the years to come.

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